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CONFERENCE CALL PARTICIPANTS

Joseph O'Dea

PRESENTATION

Operator

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Joseph O'Dea

Good day, everyone. I'm Joe O'Dea, the multi-industry analyst at Wells Fargo. Thank you for joining us today. We're very pleased to continue the presentations with Stanley Black & Decker. And from the company, we have CEO, Jim Loree; as well as Lee McChesney, who is the Vice President of Corporate Finance, and the CFO of the Tools & Storage segment as well as Dennis Lange, who is the Vice President of Investor Relations. So thank you all for joining us today.

We're going to kick things off with some opening comments from the company. So Jim, I will turn it over to you, and then we'll go into Q&A.

James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

Thank you so much, Joe. And it's great to be here at your conference. It's great to be out to tell our story and, most importantly, answer any questions that you folks may have. Let's start by just with a quick overview of the company. Today, it's about a $14 billion, $15 billion revenue company as of 2020, and that's going to change, I think, pretty dramatically in 2021 with great growth, it looks like. Market cap running around $34 billion, about 53,000 employees. And a cash dividend yield right now of about 1.3%.

3 segments, Tools & Storage being perhaps largest and most widely discussed and understood. It is the franchise, the global tools franchise to own in the world. Last year, sales was around $10 billion, revenue was around $10 billion. And fantastic brands, Craftsman, DEWALT, Black & Decker, Stanley, really stable of -- incredible iconic brands and only tool company to participate in all 4 end markets: construction, DIY, automotive and industrial repair, and only tool company to have very large franchises in both power tools and hand-held tools.

Some of the other power tool players have a few hand tools and so forth. And some of the hand tool players have some power tools, but we have significant businesses in both. There's 2 other segments. There's a Security segment, which is the #2 commercial security services provider in the world. Does installation, monitoring service for commercial security systems.

And then there's an Industrial segment, which has a fantastic Engineered Fastening business, also a significant Infrastructure business and is coming out of a -- into a really nice part of the industrial cycle right now and has some great future ahead of it also in terms of electrification of automobiles and increased content, which I expect we'll probably get into at some point during this session.

So let's go to the next slide, please. What I'm focusing on today and will be in our investor meeting next week as well is the tremendous areas of growth catalysts that we have. So we are experiencing exceptional growth right now based on how the pandemic has resorted out the owners'

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reconnection to the Home & Garden and a whole series of different aspects related to the pandemic, but also we've been -- spent several years repositioning our portfolio in the company to really drive growth hard.

We've had a 9% growth CAGR over the last -- revenue growth CAGR over the last 20 years, and it's been a combination of acquisitions and organic, and it's been a really great long-term growth formula.

So what's ahead of us now, and we could talk about some of the things that we did that are now bearing great fruit such as the Craftsman acquisition, which we did a few years ago, and also we did a lot of sorting out the brands in different channels of retail. So working with our big home center partners. We have big businesses at both Home Depot and Lowe's.

And then we have a very strong e-commerce franchise, which grew about 40% last year. And at the moment, in the first quarter, for example, grew almost 100%. That's a 1 -- last year it was a $1.8 billion business. So really well positioned in the e-commerce channel and, of course, the pandemic has made that incredibly important.

We have a very innovative product line in our power tools in our hand tools business. We have innovations such as FLEXVOLT, DEWALT XTREME, DEWALT ATOMIC and the whole XR series of 20-volt tools. We have a major initiative going on to revitalize the Black & Decker brand, which will become a much more e-commerce-focused brand focused on millennials and Gen Z generations, become more of a lifestyle brand than a power tool brand, and that's exciting.

I talked about Engineered Fastening and the lightweighting opportunity ahead of us with electric vehicles and then our Security business is in the middle of a transformation and the increased focus on health and safety that exists in today's society plays very well to that business.

So lots of great things going on, multibillion-dollar growth opportunities ahead. We have an acquisition that we're going to be making, it looks like in the back half of this year. We have an option to acquire 80% of MTD. MTD is an Ohio based family-owned company. We own 20% of that now.

And we have an option, beginning in July, to buy the remaining 80% with an all-in EBITDA multiple of about 7x to 8x. And that company has about almost a $3 billion franchise in outdoor power equipment, selling into both home centers and retail channels in the United States and to some extent, in Europe as well as selling into the pro channel.

And what we intend to do with that is bring our knowledge and know-how in electrification to that market, and we intend to be the catalyst to electrify the outdoor power equipment market in the United States, in particular. And we are positioning ourselves to do that right now. Also a very innovative company, the one that will fit as a wonderful adjacency to our portfolio.

So with that, Joe, I think I'll turn it back to you and take it wherever you want to go.

QUESTIONS AND ANSWERS

Joseph O'Dea

All right. Terrific. Thanks, Jim. And for those following along, my e-mail address is Joseph.Odea@wellsfargo.com. You should see that on the bottom of your screen as well. So please feel free to e-mail me with any questions, and I'm happy to weave those into the discussion.

Jim, I think to kick things off in terms of some of the major themes and the reconnection with Home & Garden that we've seen. And I think the commentary we've heard seems to be getting incrementally constructive around the idea that this is structural rather than event-driven.

And can you talk -- a couple of questions around this. But first, in terms of what you're tracking? What's the data that you're looking at that informs a view around this being a more lasting kind of transition?

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James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

There's a number of different data points. One of the things we did a fair amount of research over the last couple of months with American consumers and try to understand what of percentage of population that we surveyed was actually recommitting to DIY on a more permanent basis.

So you have that. It came out that it was a very significant percentage, something like 75% of the population who had done at least 1 DIY project and rediscovered, in some cases, DIY. But we also know that there is a tremendous tailwind building in the housing and both new homes and existing homes. We expect to hit the 1.2 million number for starts in 2020, looks like we're tracking well to that. And 2022 and 2023 look pretty good, too, and we may actually even surpass 1.2 million in terms of single-family starts. So you have that.

And then you have all this repurposing that it's going on. People want bigger and better work environments in their home. They want to be able to separate their work life from their home life. And we do know that there's this tremendous tailwind growing in terms of hybrid working models. And so whether you're at home 100% of the time or whether you have a hybrid model, you need to have a home where you can actually separate yourself from working -- your work life from your home life during work hours.

So we know that's going on, and we also know that there's a lot of commercial repurposing going. And in fact, we're in the temporary quarters right now because we're repurposing our headquarters to basically provide the capability to be a hybrid work environment. So that's all good. We see what's going on in outdoor. In outdoor, people are spending more time in their gardens, on their ground. They're buying a lot of products. The outdoor business was up 120% in the first quarter. So this gives you some sense for that.

And I think the other thing is the shift to e-commerce. I think that's going to be a secular -- I mean it was a secular trend. I think it's just an accelerated trend now. Last year, we went from 12% of our tools revenues in e-commerce to 18%. Last year, we went from 12% the prior year to 18% last year. And this year, it's going to be even bigger. E-commerce was up almost 100% in the first quarter. We have $1.8 billion business last year in that.

So just a lot of indications that the growth will continue, not to mention just the absolute incredible amount of stimulus that's being provided by governments around the world, which is fueling GDP in our business to some extent, also attracts benefits from GDP growth, as you might expect.

Joseph O'Dea

And I imagine there are some investments that you'd like to make that hinge a little bit on the outcome of what is the underlying normalized demand and making a call on kind of the structural durability of some of what we're seeing right now. What do you think the time line is to -- when you'll feel that much more comfortable that this is durable and then start to make some of those adjustments in terms of the foundation of the business?

James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

Yes, we've crossed the rubicon on that one. We're investing $200 million of organic investments, not to mention, CapEx investments, which, for instance, bringing 3 plants on, this year, 2 in Mexico, 1 in the United States with investment over $100 million in those plants.

And we've gone out to our supply base and worked on capacity to make sure that we have capacity to serve. We're working on as much as $3.5 billion per quarter of capacity. So I think we're putting our money where we're able to here. And we are reinvesting at a very high rate and still generating a record operating margin. So 17.6% in the first quarter was a record operating margin for the first quarter for the company. And we are well into these investments at this point in time. So a lot of that is actually in the run rate.

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Joseph O'Dea

And then moving on to recent performance and the considerably strong growth that we saw in Tools & Storage in the first quarter with a 45% organic growth in global strength. But on top of what is underlying kind of strong end-market growth, you're outperforming at what sounds like a pretty impressive clip with maybe half of that growth that you saw in the first quarter attributed to outperformance.

Can you expand on some of the factors that are driving some of that? I know the innovation is a cornerstone of the company. But why we would see some of that coming together? And also speak to the durability of those gains.

James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

So contrary to what a number of people think, it truly is a global phenomenon. And I think we benefit greatly from the ubiquity of our channel presence. And -- including e-commerce, by the way. So we have great products, great brands, full access to all the channels and great commercial people. And we have a lot of demand. So when you think about the growth, 41% in North America last quarter, 47% in Europe, 77% in Latin America. 77% in Brazil, 60-plus percent in Asia.

I mean it's -- this is not just, hey, Home Depot is open or Lowe's is open. So let's go. Unfortunately, we have -- this is a global phenomenon, which is I think a confluence of a great demand picture, and then a lot of hard work that we've done over the years getting our brands lined up in the right places, getting our -- building out our distribution, building out our e-commerce channel and great innovation to sell to the end users and right place at the right time.

Joseph O'Dea

And you touched a little bit on e-commerce there. And so just to shift over to the e-commerce side of things. We've seen that quickly go from a low mid-teens percent of sales up to a high teens, nearly 20% of sales. And where do you see that going? As you think about the next few years, what is the opportunity there? Is there any kind of giveback of that as things normalize and we see reopening? Or do think you that it just continues to march higher?

James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

Well, I think it continues to march higher. It'll probably much higher at a lower rate, is what I expect. And it will reach a practical limit at some point in time because people do like to go touch and feel products. I think we'll see more of an omnichannel approach as we go forward. But for us, one of the benefits, I suppose, of having this global footprint is that we are pretty much in every major economy in the world but -- and there's a couple of markets where we're under-indexed for share, including Germany, including India and China, which are very important markets as you'd appreciate. And Japan. So in those markets, we have the capability with our e-commerce strategy to actually go direct-to-consumer and break down these ossified distribution channels that we have always had difficulty penetrating because we have such great products.

And in those channels, when you have brands that are recognizable and great innovation, and even though you may have some trouble breaking through some -- or the traditional channels, e-commerce will enable us to do that very efficiently and in a very disruptive manner. And so I think that will help fuel the growth of e-commerce as we go.

Joseph O'Dea

And I think if you step back and think about Tools & Storage market share, the e-commerce market share index is higher than the overall segment itself. Do you see that as a first-mover advantage that you can build on and how you go-to-market through e-commerce and the various resources that you have? Or do you see an industry that's calling really hard to try to catch up with some of the advantages you have right now?

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James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

I think the industry is definitely going to move in that direction. There's no doubt about it, but I talked about those reinvestments. And we decided -- we have about a 3:1 advantage in terms of relative market share in the e-commerce channel around the globe versus the next closest competitor. And we decided, as we got into the pandemic, we started making reinvestments in the latter part of last year to really double down on e-commerce. So that recognizing that there would be a thrust from the competition to get involved in e-commerce in a much more intensive way.

So we have brought in experts that understand e-commerce as well as anybody outside of the industry. And then we have our industry people that have been doing this for now for 10 years, building the business up from $100 million in 2010 to almost $2 billion last year and growing at a great rate. So we have doubled down in terms of our resource investment, and we're taking it very seriously. And it's a big part of our go-forward strategy.

Joseph O'Dea

And then I want to pivot to electrification. And when you think about -- you're seeing that as an opportunity across a lot of parts of the business. But when you step back, some of this can be a transition of technology, and some of this can be a revenue pie expander. I think auto might be an example of that. But can you talk about parts of the business where you see electrification as a technology adoption that's going to give you a bigger revenue opportunity?

James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

Sure. I think there's -- outdoor for sure is perhaps the largest. And you think about getting such a great leading company like MTD with its expertise in -- and almost $3 billion of revenue and its expertise in riding mowers and zero-turn mowers and push mowers, but they're largely all petrol fueled. And our expertise in battery control systems and motors, and our access to technology in that regard. And MTD has the manufacturing footprint to make these lawn mowers. And also the knowledge of blade, engineering, air flow engineering and lightweighting, which they've been working on for a couple of years now and autonomy. And we can put together unbeatable products. And we have a pipeline of what I would consider to be unbeatable products.

And then you marry that with the brands that we have -- and MTD has been disadvantaged in the sense that their brands are good, but they're not DEWALT. They're not Stanley, they're not Black & Decker and so forth and Craftsman.

So the combination of that is going to give us the wherewithal to get a great growth story out of electrification, which will occur. And a lot of people don't know this, but the small gas engines are very big polluters because they don't have the same emissions technology that the automotive engines have. So you get a big improvement of carbon emissions from electrifying outdoor power equipment.

So that's a multibillion-dollar opportunity. And then the other one is the electric vehicles. So today, our Engineered Fastening business has about $10 of content -- fastener content per vehicle. And our footprint is all over the world, of all the other OEMs, pretty much all the OEMS, most of the OEMs in the world. And so we install, we sell the systems to install the fasteners, and then we get a recurring revenue stream from the fasteners of about $10 per car.

When we -- when that market shifts to electric, we have about somewhere between $30 and $60 of content in an electric vehicle versus a petroleum-fueled vehicle. And so our automotive business today is roughly close to about $1 billion. And so when you start thinking about the content increases that are going to occur over time, that becomes a material revenue driver over the medium-term for us as well.

Then the last one is not so much of a revenue driver. I know that's what you asked for, but it is an opportunity for us to make power tools out of recyclable materials and recycled and/or recyclable materials. That probably won't be a massive revenue driver, but it certainly will be a great brand reputation driver for us as we go forward.

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Joseph O'Dea

Quickly on that point. Is that cost competitive with the current approach? Or is there any kind of margin impact when you go to a more environmentally sound approach to doing it?

James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

It's a little bit like shopping in the Whole Foods, where you have the organic foods, and then you have the regular. And the organic costs a little more, but there's a lot of people that want it and buy it.

It's going to be the same thing with the recycle, the power tools made out of water bottles, for example, it's going to cost more, but not prohibitively more, and it won't be a lower margin. But we're trying to get closer.

Joseph O'Dea

And then just on a sequencing, as it relates to electrification, where do you see that kind of momentum building earliest in terms of the new opportunities that are in front of you across the business? Where do you think you'll start realizing that soonest?

James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

So if you think of this market in segments, you have the handheld, which is what we have today. And handheld has a whole array of power requirements, whether you're talking about a chainsaw or a hedge trimmer or a one of those little grass shears or whatever. So the handheld today it's about 50% or electric. And so I think that isn't migrating at a very fast pace because technology that we have in the market today enables us, such as FLEXVOLT, enables us to go up the power curve and into the professional-grade tools, which we're doing, actually we have some in the market this year as we speak.

And so that's the fastest. So then you have the push mowers, which is also going to happen pretty fast because the ability to achieve decent run time and with good power is increasing as well in that regard. And then the last one, which will be the riders and the zero-turns, that will be a little bit slower, I think. But give it 5, 6 years, that will flip, too.

Joseph O'Dea

And then somewhat related to the comment around you get pricing ability when you go to something like using recyclable inputs. And a pricing-related question in terms of you're looking at a year where we're seeing some inflationary headwinds. We go back to the 2017, '18, '19 period of time, clearly, very challenging in terms of inflationary headwinds. We haven't seen you price aggressively, right? It's about 1 point of price, a year kind of thing, even when it looks like a difficult input cost environment. What is it about given the brand power, obviously, the strength of the company, what's the pricing philosophy? Why don't we see maybe a little bit more flexing of pricing power that you could have out there?

James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

Time to get the finance people way in.

Lee B. McChesney - *Stanley Black & Decker, Inc. - VP Corporate Finance & CFO of Tools & Storage*

Joe, I would say, first of all, just be a little cautious on the price calculation. There's the pricing is defined by the accounting team. So it's primarily year-over-year differences on what we've sold. So if you sold something last year, you sell it lower, more, you get the difference. But there's a whole world going on in gross margin. If you certainly look at our gross margin trend, we are doing very well.

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So an area, for example, would be new product development. So when we bring new product to the market, it's an ideal time to really reset that marker. And if you do that with a better product, better features and then you obviously have an opportunity with the customer to reset price points. So that's a big part of the element as well.

And one of the things we've done with margin resiliency is build out a really strong pricing COE, and out of that can come a lot of focus on mix. So mix on promotions, mix on who we sell to, where we sell. And that's why you're seeing the gross margin rate improve significantly over the last 1.5 years for us. So it is a core capability. We are in a way better place than we were before. And that's why when we look forward and we see an inflationary environment, we're confident that we can offset that with continued strong price actions and then building out other elements of margin resiliency.

Joseph O'Dea

And then with a few minutes we have left. Let's pivot to innovation. Obviously, the core strength of the company, you have a Growth Summit event coming next week, which we're excited for. Can you talk about the pipeline, what the pipeline today for the next few years looks like versus what it was like over the past few years?

And within that, if you could distinguish between what would be kind of the core pipeline? And then I know the breakthrough pipelines and what that might look like as well?

James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

Yes. I mean, I can't get that much into innovation. It isn't out in the market because I have a very aggressive competitor who likes to copy a lot of what we do. So I'm not going to speak about up and coming breakthroughs.

But I will say that we've had a number of terrific innovations over the last few years, and we have not slowed down a bit, and there's more to come here sooner than later. But we've already had -- I talked about it earlier, the FLEXVOLT, the ATOMIC, the EXTREME, and now FLEXVOLT ADVANTAGE and POWER DETECT. So all those are in power tool innovations. And they, I guess, over a 4-year period, there's over $1 billion of revenue that can be attributed to those product lines. And it's all -- lot of the innovation that's come, FLEXVOLT was great. The multi-voltage battery, but also leveraging the combination of control technology, motor technology and DC brushless motors and creating more power, more run time, more power in a smaller tool. And so that's been one of the themes.

You're going to see a land slide of innovation coming from the MTD business where we really are going to shake up the industry with innovation, it will be exciting to watch. And more to come on that front soon.

Joseph O'Dea

Terrific. Well, unfortunately, I think that actually brings us to the end of the time. But really appreciate the commentary and the thoughts. Certainly looking forward to the event next week. I guess that means that you won't be making too many product announcements necessarily to prohibit people following in your footsteps there too closely. But we do appreciate it. So Jim, Lee, Dennis, thank you so much for joining us. And take care.

James M. Loree - *Stanley Black & Decker, Inc. - CEO & Director*

Thank you, Joe.

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